(4)

No. 95-1542

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1995.

LELAND A. COOPER, ET AL.,
Petitioners,

v.

COMMISSIONER OF REVENUE
OF MASSACHUSETTS,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT OF MASSACHUSETTS

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTION PRESENTED

Does a State violate 4 U.S.C. § 111 (1994)(prohibiting discriminatory taxation of federal officers and employees), when it taxes income received from state, local and federal non-contributory pensions, and exempts only contributory state, local and federal pensions?

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IN THE
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LELAND COOPER, et al.,
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v.

COMMISSIONER OF REVENUE
OF MASSACHUSETTS,
Respondent.

On Petition For A Writ of
Certiorari To The Supreme Judicial
Court of Massachusetts

RESPONDENT'S BRIEF IN OPPOSITION

Pursuant to United States Supreme Court Rule 15, the Commissioner of Revenue of Massachusetts submits this brief in opposition to the petition for a writ of certiorari filed by Leland Cooper, et al.

JURISDICTION

Petitioners invoke the jurisdiction of this Court pursuant to 28 U.S.C. § 1257, to review a final judgment of the Massachusetts Supreme Judicial Court dated December 26, 1995.

STATUTORY PROVISIONS INVOLVED

In addition to 4 U.S.C. § 111, quoted in the petition for a writ of certiorari at 2, the following sections of the Massachusetts General Laws are involved:

> Mass. Gen. Laws Ann. c. 62, § 2(a)(West 1988):
>
> Massachusetts gross income shall mean the federal gross income. . . . with the following further modifications:--
>
> (1) The items to be added thereto are:--

* * *

> (I) Amounts contributed on behalf of the taxpayer pursuant to [the state and municipal pension statute], subdivision (10) of section twenty-two of chapter thirty-two or pursuant to [the judges retirement statute], paragraph (I) of section sixty-five D of said chapter thirty-two and not included in the federal gross income. . . .
>
> (2) The items to be deducted therefrom are:--
>
> * * *
>
> (E) Income from any contributory annuity, pension, endowment, or retirement fund of the United States government or the commonwealth or any political subdivision thereof, to which the employee has contributed.

STATEMENT

Massachusetts General Laws c. 62, § 2(a)(2)(E) exempts from the Massachusetts income tax "[i]ncome from any contributory annuity, pension, endowment or retirement fund of the United States government or the Commonwealth or any political subdivision thereof, to which the employee has contributed." *Id.* (emphasis added). It is undisputed that this

exemption benefits all state and federal retirees who receive income from "contributory" pension funds. Pet. App. A.4. It is also undisputed that the military pensions at issue are not "contributory" pensions. *Id.* The issue in this case is whether the Massachusetts income tax imposed on pensions received by military retirees nevertheless discriminates against federal officers and employees, in violation of 4 U.S.C. § 111.

Statement of Facts

Petitioners ("the taxpayers") are all residents of the Commonwealth who received income from United States military retirement benefits for some or all of the Massachusetts tax years 1986 to 1992. Pet. App. A.4. The taxpayers "are beneficiaries of a 'noncontributory' [retirement] system funded entirely by their employer, the Federal

government." *Id.* All of the taxpayers paid Massachusetts income taxes on their income from their military pensions. *Id.*

The taxpayers filed applications for abatement of income taxes paid during the tax years 1986 through 1992. *Id.*; *see* Mass. Gen. Laws Ann. c. 62C, § 37 (West 1988). The Commissioner denied the abatements. *See id.* The taxpayers appealed to the Massachusetts Appellate Tax Board (the Board). Pet. App. A.1. The Board affirmed the Commissioner. *Id.*; see Mass. Gen. Laws Ann. c. 62C, § 39 (West 1988); c. 58A, § 7 (West 1988). The Board stated that the parties had "raised no issue of law or fact that were not addressed and disposed of by the Supreme Judicial Court in *Filios* v. *Commissioner of Revenue*, 415 Mass. 806, *cert. denied*, 114 S.Ct. 1538 (1994). . . ." Pet. App. A.1. Accordingly, the Board granted the Commissioner's "motion for judgment on the pleadings." *Id.*

The *Filios* case cited by the Board arose as follows. In response to a request for an opinion submitted by various military organizations, the Commissioner issued a ruling on February 16, 1989, that military retirement benefits are taxable income under G.L. c. 62 because they are includable in federal gross income and not "contributory" within the exemption established by G.L. c. 62, § 2(a)(2)(E). Mass. Letter Ruling 89-1, 2 Official Mass. Tax Guide at 765-767 (West 1996).

On March 28, 1989, this Court issued its decision in *Davis* v. *Michigan Department of the Treasury*, 489 U.S. 803 (1989). On May 10, 1989, the Commissioner issued "Technical Information Release 89-6." Pet. App. A.5. See 830 Code of Massachusetts Regulations (C.M.R.) § 62C.3.1(7) (1993 ed.)(Technical Information Releases). The Commissioner opined that "[a]ny federal retirement income is exempt from Massachusetts tax if the system is contributory

and the employee actually contributed." 2 Official Mass. Tax Guide at 384-385 (West 1996).

At various times in late 1989 and 1990, the Commissioner denied each of the applications for abatement filed by the *Filios* plaintiffs. The taxpayers appealed to the Massachusetts Appellate Tax Board, which upheld the Commissioner's decision.

The Supreme Judicial Court affirmed the Board. *Filios* v. *Commissioner of Revenue*, 415 Mass. 806, 615 N.E.2d 933 (1993); Pet. App. A.4. The Court agreed with the Commissioner and the Board that the distinction in Massachusetts tax law between contributory and non-contributory pensions "creates significant differences between the two classes of taxpayers such that differential treatment does not violate 4 U.S.C. § 111." 415 Mass. at 809, 615 N.E.2d at 935. It concluded "that the distinction between contributory and noncontributory pensions systems was a valid

one," which did "not impose the tax based on the source of the income" and was not discriminatory. 415 Mass. at 812, 615 N.E.2d at 936. This Court denied certiorari. 114 S.Ct. 1538 (1994).

The Supreme Judicial Court in this case declined "to overrule *Filios*. . . ." Pet. App. A.4. It held that "Massachusetts tax law distinguishes between contributory and noncontributory retirement plans, not between State and Federal retirees." Pet. App. A.5. The court noted that a "State worker is required to make regular, State-taxed, contributions to the retirement system in order to get a State tax-free pension on retirement."[1] *Id.* at A. 6. "The [federal military retirees]

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[1] Citing Mass. Gen. Laws Ann. c. 32, § 22(10)(West 1989), the amicus briefs of the United States below (at p. 7) and in this Court in *Filios* (at p. 6) consistently make the mistaken representation that state employees no longer make pension contributions. The Massachusetts statute in question simply takes advantage of the tax *deferral* option under 26 U.S.C. § 414(h)(2), but the funds in question remain employee income under § 414(h)(2) (and under state law, Mass. Gen. Laws Ann. c. 62 § 2(a)(1)(I)). The opportunity to defer

made no such contribution." *Id.* Accordingly, the Court held that the Massachusetts statutes do not violate 4 U.S.C. § 111 because they do not discriminate against a federal "officer or employee because of the source of the pay or compensation." *Id.*

The petition for a writ of certiorari was filed on March 25, 1996.

SUMMARY OF REASONS FOR DENYING PETITION

1. There is no conflict among federal circuit courts, state courts or decisions of this Court. Nor does any tension exist between Massachusetts' taxation of pensions and the non-discrimination principles of 4 U.S.C. § 111.

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taxation of an employee's income until retirement or separation from state service does not change the fact that the income belongs to and is taxable to the employee. *see Howell* v. *United States*, 775 F.2d 887, 889-90 (7th Cir. 1985).

Massachusetts taxpayers may deduct income from federal (as well as state and local) pensions for state income tax purposes, if the pension plan is contributory and the taxpayer has contributed to the plan. Massachusetts does not discriminate because of the source of the income; it distinguishes solely between contributory and non-contributory public plans.

2. The decision below does not present any issue of national significance. Petitioners cite a "grandfather clause" solely in Massachusetts law for persons now living, if any, who were employed as police and fire employees in Massachusetts in the mid-1930's who elected not to join the contributory system enacted at that time. The court below correctly held that even assuming that such a person were still alive, the statutory treatment of this small, finite class did not discriminate against federal retirees in violation of 4 U.S.C., § 111. Similarly, petitioners' argument that Massachusetts' state pension system is 10% contributory merely shows that,

like any contributory system, the Massachusetts plan involves contributions by the employer as well as employees. Nothing in this arrangement shows any discrimination against federal pensioners.

REASONS FOR DENYING PETITION

Under Supreme Court Rule 10, "review on Writ of Certiorari is not a matter of judicial right but of judicial discretion," and "will be granted only where there are special and important reasons therefor." The purpose of certiorari writs is to permit the Court to select cases of "such gravity and general importance" as to warrant full court review. *In Re Woods*, 143 U.S. 202, 206 (1892). For the reasons stated below, the petition does not satisfy the criteria that guide the Court's discretion to review a case. Accordingly, the petition should be denied.

I. THE COMMONWEALTH'S TAX STATUTES CONFORM TO THE FEDERAL ANTI-DISCRIMINATION STATUTE.

In the conceded absence of a conflict between decisions of the federal courts of appeals, state courts, or this Court,[2] the only question is whether petitioners have raised an issue of national importance. Their sole argument to that effect is based upon an alleged violation of 4 U.S.C. § 111.

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[2]Other decisions upholding state statutes against a challenge under 4 U.S.C. § 111 include *Brown* v. *Mierke*, 443 S.E.2d 462, 467 (W. Va.), *cert. denied sub nom., Brown* v. *Paige*, 115 S.Ct. 207 (1994)(upholding favorable treatment of a narrow class of former state and local employees, where military retirees were treated more favorably than many civilian and state retirees and were treated equally with some public employees); *Witte* v. *Director of Revenue*, 829 S.W.2d 436, 438 (Mo. En Banc 1992)(state tax did not single out state employees for favorable treatment, where many federal employees received the same tax treatment and the state tax did not unduly interfere with federal operations); *Alarid* v. *Sec. Of* N.M. Dept. of Tax. and Rev., 118 N.M. 23, 878 P. 2d 341 (Ct. App.),*cert. denied*, 118 N.M. 90, 879 P. 2d 91 (N.M. 1994) *cert. denied*, 115 S.Ct. 733 (1995).

The question under 4 U.S.C. § 111 is whether the Massachusetts system discriminates against the plaintiff taxpayers "because of the source of the pay or compensation." This clause codifies the nondiscrimination component of the federal constitutional doctrine of intergovernmental tax immunity, which "barred taxes that operat[e] so as to discriminate against the Government or those with whom it deals." *Davis*, 489 U.S. at 812 (quoting *United States* v. *City of Detroit*, 355 U.S. 466, 473 (1958)).

During the tax years at issue in this appeal, Massachusetts permitted the deduction from gross income from any contributory "retirement fund of the United States government." Massachusetts thus permits deductions not only by state contributory retirees, but also by "federal retirees who contributed to their benefits, such as members of the Central Intelligence Agency, Foreign Service, bankruptcy judges and United States magistrates." *See Barker* v. *Kansas*, 503 U.S.

594, 605 n.5 (1992). *See also* Mass. Dept. of Rev. Letter Ruling 83-38, reprinted in Off. Mass. Tax Guide at 652 (West 1996)(exemption for contributory annuity received by civilian employee of the Army and Air Force Exchange Service).

A tax on non-contributory pensions, combined with an exemption for contributory pensions, simply does not discriminate against the federal government or its employees. Contributory federal pensions receive the same treatment as contributory state pensions. G.L. c. 62, §§ 2(a)(1)(I), 3.B(a)(4), discussed above, pp. 3-4. This fact pattern does not bring this case within recent decisions of this Court striking down state taxation laws. Neither of the cases cited by petitioner involved a consistently-applied distinction between contributory and non-contributory pensions, regardless of their source. *Davis*, 489 U.S. at 805; *Barker*, 503 U.S. at 605 n.5.

Davis, 489 U.S. at 816, and *Barker*, 503 U.S. at 598, held that States may lawfully tax pensions differently if there

are "significant differences" between the pensions. A retiree who contributed to a pension plan paid consideration and has her own money funding the system, while a non-contributory retiree does not. In practice, in Massachusetts, there is an additional difference, namely the exposure of the employee's contributions to state taxation at the time of the contributions, through inclusion in Massachusetts gross income. If "significant differences" do not include distinctions based upon employees' payment of consideration to the employer's pension fund plus payment of income tax, then it is hard to imagine what differences might be considered significant enough to warrant different treatment of classes of pensions. At the very least, "[p]rinciples of federalism" require Congress to speak more clearly than it has here, if it intended to set such novel and strict "limits upon the taxation authority of state government, an authority [the Supreme Court has] recognized

as central to state sovereignty." See *Department of Revenue of Oregon* v. *ACF Industries, Inc.*, 114 S.Ct. 843, 850 (1994).

In short, unlike Michigan and Kansas, Massachusetts exempts all federal contributory pensions from state taxation. Since state and federal contributory systems are treated equally, as are non-contributory systems, there is no discrimination or inconsistent treatment, and § 111 does not come into play. *See Werner Machine Co., Inc.* v. *Director of Division of Taxation*, 350 U.S. 492, 493-94 (1956)("Since the tax remains the same whatever the character of the corporate assets may be, no claim can be sustained that this taxing statute discriminates against the federal obligations.") *Doneski* v. *Comptroller of the Treasury*, 91 Md. App. 614, 605 A.2d 649, 656 (1991), *cert. denied*, 327 Md. 523, 610 A.2d 796 (1992), *cert. denied*, 506 U.S. 1054 (1993).

II. PETITIONERS' ATTACKS ON THE MASSACHUSETTS TAX SYSTEM DO NOT INVOLVE QUESTIONS OF NATIONAL IMPORTANCE AND RAISE ISSUES OF STATE LAW.

1. The taxpayers assert (Pet. at 12-13) that Massachusetts' system is not contributory because the benefit levels are, allegedly, funded 90 percent by the state and approximately 10 percent by employee contributions (Pet. at 13). This argument appears to depend upon splitting the state benefits into two components--one contributory and one non-contributory. But state law, as applied by the Supreme Judicial Court in this case, treats the entire benefit package as one pension. *See* Pet. App. A.6. To the extent that petitioners argue otherwise, they are merely disagreeing with the state's highest Court on an issue of state law.

The Commonwealth's approach, in any event, is consistent with the usual understanding of the phrase

"contributory" pension, in which "employees, *as well as employers*, make payments to a pension fund". Black's Law Dictionary (6th ed.), p. 329 (emphasis added). *See* generally 29 U.S.C. §§ 1054(c), 1056(c)(ERISA provisions contemplating employer contributions); Canan, *Qualified Retirement and Other Employee Benefit Plans*, § 3.51, pp. 135-136 (West Publ. Co. 1992).[3]

Under the state law definition of contributory plan set forth in the Commissioner's Technical Information Release ("TIR") 92-3 the question is whether employee contributions are included in Massachusetts gross income. Massachusetts *does* include the pension plan contributions of its state and local employees in gross income for state tax purposes. Mass.

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[3]Based on the figures in *Hogan* v. *United States*, 513 F.2d 170, 172 (6th Cir.), *cert. denied*, 423 U.S. 836 (1975), it appears that federal employees once contributed only $10.3 billion (½ of the funded liability of $20.6 billion), which was only 13 percent of the total pension liability of $78.3 billion.

Gen. Laws. c. 62, § 2(a)(1)(I), quoted above, pp. 2-3. The state taxation system under attack here thus treats the contribution consistently as being paid from the state and local employees' income. Petitioners concede as much (Pet. at 15 and n. 10). The fact and degree of participation by the employer in funding benefits therefore is irrelevant. Any other conclusion would make legality under § 111 turn upon two moving targets: the percentage contribution by federal workers and by State workers, respectively. Such a fact-bound issue is not appropriate for Supreme Court review.

In short, petitioners have not provided any basis for disregarding the fact, found by the court below, that the exempt state (and local) pensions are contributory, and their pensions are not.

2. Petitioners also argue that there exists an obscure exemption for certain police and fire employees, if any, whose employment predated the 1930's and 1940's. It is

an enormous stretch for petitioners to call this a "state policy" of exemption. Indeed, petitioners' failure to allege more than a "small and dwindling" class of exempt retirees, even in Massachusetts (Pet. App. A.8), leads directly to the conclusion that this issue is not "significant," let alone one of national importance such as to warrant review by this Court.

The state provision in question exempts from taxation any pension received on account of service by local "police and fire department" employees who were so employed before establishment of the contributory retirement system *and* who did not elect to join the contributory retirement system. Mass. St. 1973, c. 876, § 1. This provision is a "grandfather clause" for police and fire employees whose employment predated the state legislation in the 1930's and 1940's that made all public retirement systems mandatory. *See* Pet. App. A.7 - A.8. Petitioners do not claim that such a provision exists in other States.

The court below held that the grandfather clause was not discriminatory under 4 U.S.C. § 111. The court explained that the clause favored a class of retirees not on the basis of the source of their pay, but "on the basis of their occupation (police and firefighters) and date of first employment (before 1938)." Pet. App. A.8. The court also found correctly that the clause "protects a small and dwindling class." *Id.* Even assuming, as did the court below (*id.* at A.7-8 n.4), that there are currently exempted retirees covered by the clause, there is simply no record proof of discrimination, much less any indication of an issue of national importance.

More generally, petitioners do not argue that the grandfather clause shows that the Massachusetts system of *exemption* for contributory pensions is in any way under- or over-inclusive. They only argue that *taxation* of non-contributory pensions is very minimally under-inclusive. The validity of state law must turn upon the overriding and

overwhelming effect of the law as a whole, that is, "the generality of cases, not the rare exceptions." *See Mathews* v. *Eldridge*, 424 U.S. 319, 344 (1976)(discussing constitutional procedural due process analysis); *Weinberger* v. *Salfi*, 422 U.S. 749, 777 (1975)(evaluating federal legislation under the rational basis test). In short, the grandfather clause and its dwindling subject class do not present issues of national importance warranting review by this Court.[4]

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[4]Finally, petitioners quote the amicus brief of the United States filed in this Court in *Filios* and argue that the decision below "would serve as a guidepost for States seeking to circumvent" 4 U.S.C. § 111. Pet. at 18. Nearly three years have passed since the decision of the Supreme Judicial Court in *Filios*; two years have passed since the Court denied certiorari in *Filios*, and the Commissioner is unaware of any State that has enacted a law similar to the Massachusetts law at issue.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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PETITION FOR WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT FOR THE COMMONWEALTH OF MASSACHUSETTS

PETITIONERS' REPLY TO THE BRIEF IN OPPOSITION

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U.S. SUPREME COURT RULES

Rule 15.6 1

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V.

COMMISSIONER OF REVENUE OF MASSACHUSETTS

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PETITION FOR WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT FOR THE COMMONWEALTH OF MASSACHUSETTS

PETITIONERS' REPLY TO THE BRIEF IN OPPOSITION

Pursuant to Rule 15.6 of the Rules of this Court, petitioners Leland A. Cooper et al. submit this Reply to the Brief in Opposition to the Petition filed in this case.

I. THIS CASE RAISES QUESTIONS OF NATIONAL IMPORTANCE.

A. The Record Before the Court.

Respondent asks this Court to deny the petition for a writ of certiorari on the grounds, among others, that petitioners' claims do not raise "issues of national importance warranting review by this Court." Brief in Opposition at 22. The record before the Court convincingly demonstrates the contrary.

Petitioners respectfully call to the Court's attention the brief amicus curiae filed by the Retired Officers Association and Twenty Two Other Military and Veterans Organizations ("TROA") with a combined membership of one million men and women who are retired, reserve or active members of the uniformed services. As ROA's brief notes, Massachusetts' policy of taxing federal military retirees' benefits, while completely exempting benefits received by state and local retirees, presents a direct threat to Congress' ability to choose how to compensate the men and women responsible for our national defense, a consideration of obvious national importance. See U.S. Const., art. I, § 8, cl. 12, 13 and 14.

Further evidence that the decision below does raise matters of national significance is the fact that the Solicitor General has filed a brief amicus curiae supporting the petition. As the Solicitor General notes, "[t]he United States has a continuing interest in ensuring that its employees are not subjected to discriminatory tax treatment." Brief for the United States as Amicus Curiae Supporting Petitioners at 2.

B. Unless Reversed, the Decision Below Will Accelerate Other States' Efforts to Circumvent 4 USC § 111 and This Court's Decisions.

The Brief in Opposition seeks to undercut the national

significance of the issue raised in this case by mentioning, in a footnote, that no state "has enacted a law similar to the Massachusetts law at issue." Brief in Opposition at 22, n.4. While that may or not be true, it avoids the more serious point. Massachusetts' policy of discriminating in favor of state employees is only the most blatant of a number of different attempts by other states to achieve the same end. Review by this Court is called for to ensure the defeat of those efforts to deny federal workers their constitutional protections.

As this Court has noted, in a case involving application of 4 U.S.C. 111, state courts have shown difficulty in accepting this Court's decisions in this area "as a controlling statement of federal law." Harper v. Virginia Department of Taxation, -- U.S. --, 125 L. Ed. 2d 74, 83-84 (1993). In the brief for the United States supporting the petition, the Solicitor General warned that "[i]f the decision in this case were allowed to stand, it would serve as a guidepost for States seeking to circumvent the clear restrictions imposed by 4 U.S.C. 111 and this Court's prior decisions." Brief for the United States as Amicus Curiae Supporting Petitioners at 7.

Evidence for the persistence of such efforts is not hard to find. For example, one Oregon judge recently noted in dissent that the Oregon Supreme Court was "approv[ing] a legislative device specifically and narrowly tailored to avoid the rule of intergovernmental tax immunity that was explicated [in Davis, Harper and Barker]." Ragsdale v. Department of Revenue, 895 P. 2d 1348, 1357 (Or. 1995)(Gillette, J. dissenting)(emphasis added). The law in that case provided for payments to state retirees intended to serve as a "partial refund of state income taxes paid by state retirees . . . " Id. at 1358.[1] Needless to say, no similar tax

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1. Oregon's ongoing effort to discriminate in favor of its retirees has apparently most recently resulted in a scheme whereby the state collects "tax" from retirees, but then pays them "damages" at the highest marginal statutory rate of tax plus 9% interest. See Or. Laws 1995, c. 569.

offsets were made available to federal retirees. A similar "adjustment," intended to protect state, but not federal, retirees from the impact of state taxes was struck down by the Montana Supreme Court. See Sheedy v. Public Employees Ret. Div., 864 P. 2d 762, 768 (Mont. 1993) (invalidating law as "a partial tax rebate denominated otherwise in an attempt to evade the requirements of federal law.")(emphasis added).

Massachusetts, like a number of other states, seems to think that intergovernmental tax immunity is some sort of game and that, so long as it is sufficiently clever, it can continue to provide its retirees with tax free retirement benefits while retaining the "cake" of taxing federal military retirees. But, as the Arizona Court of Appeals recently noted in striking down yet another state tax law as violative of 4 USC § 111:

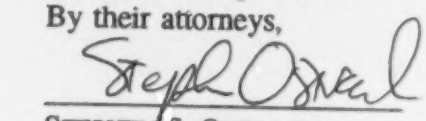
> [w]hat defendants' reasoning ultimately boils down to is that indirect discriminatory taxation that is not specifically intended to operate as such, is not discriminatory at all. Defendants cite no authority that would support this idea in the tax arena, and we are aware of none.

Kerr v. Waddell, 899 P. 2d 162, 176 (Ariz. App. 1995), remanded on other grounds, 1 CA-Tax 92-0010 (Ariz. App. Apr. 23, 1996)

CONCLUSION

For the foregoing reasons and for the reasons stated in their previously filed petition, petitioners request that their application for a writ of certiorari be granted and that, after hearing, the December 26, 1995 decision of the Supreme Judicial Court of the Commonwealth of Massachusetts be reversed.

Respectfully submitted,
Leland A. Cooper et al.
By their attorneys,



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